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What This President Isn't Telling You About Social Security

"What should we do with this projected surplus? I have a simple four-word answer: Save Social Security first. . . . I propose that we reserve 100 percent of the surplus — that's every penny of any surplus — until we have taken all the necessary measures to strengthen the Social Security system for the 21st century."

[President Clinton, State of the Union Address, 1/27/98]

Like much of what this president has said recently, his four-word pronouncement on use of the budget surplus is open to interpretation — ranging from politically clever to economically meaningless. However, it shouldn't be passed off simply as soaring rhetoric because it contains two big problems: a lie, and a "doability" factor. First, the lie: Clinton flat out contradicts himself on use of the surplus — claiming he wants to save "every penny" of it, while proposing billions in new spending in his budget. Now the doability part: Given how Social Security's trust fund operates, today's budget surplus *cannot* be set aside for Social Security's future liabilities. And nor can Congress simply amend the law to make it so.

That's what he didn't tell you. And so we have a president surreptitiously spending the surplus out from under Social Security while simultaneously avoiding substantively dealing with Social Security — yet will claim to have led the "save Social Security" effort.

Problem One: Clinton Has Already Proposed to Spend Some of the Surplus

Essentially, Clinton has constructed a wonderful political scenario for himself and his party: he holds the budget surplus hostage until the Republican-controlled Congress deals with Social Security. In the meantime, he gambles that the individually small but cumulatively large new spending initiatives in his budget — \$150 billion over the next five years, according to the Senate Budget Committee — prove irresistible.

Not only does the President's latest budget propose \$150 billion in new spending, but his budget violates last year's budget agreement. "The Administration is not following the rules," said June O'Neill, CBO director [*Congress Daily*, 2/6/98]. According to the White House's own estimates, the President's discretionary spending breaks the spending caps by \$37 billion. Clinton's plans for new spending therefore violate both last year's budget agreement and this year's promise to save "every penny of any surplus..." for Social Security. Without his new spending, there would be an additional \$150 billion in that surplus he claims to be saving first for Social Security.

Problem Two: 'Saving the Surplus for Social Security' is Meaningless

Neither Clinton nor anyone in his administration has yet offered an explanation, much less a proposal, as to how actually saving the surplus to fund future Social Security obligations is to be accomplished. Substantively it is meaningless, as an analysis of the Social Security program demonstrates. Simply running a surplus in the federal budget today does nothing to help address Social Security's problems tomorrow.

Social Security operates (and always has) on a pay-as-you-go basis: Current revenues from the payroll tax pay for current benefits. The often-mentioned trust fund is merely a bookkeeping device that records the operations attributed to the Social Security program. The only assets it holds (by law) are special government securities. These securities must of course be redeemed in cash (when in the near future Social Security begins to spend more than it receives in revenue), which requires the government to run surpluses or borrow at the time of redemption. Current surpluses are therefore meaningless since they don't help future shortfalls. To say otherwise is simply not true.

How Our Social Security System Works: *Current Surpluses Can't Offset Future Social Security Deficits*

This year, CBO projects the Social Security trust fund balance to look as follows:

- It will receive total income of \$479.7 billion: \$417.3 billion in tax revenue and \$46.5 billion in interest.
- It will disburse \$371.8 billion in benefits and \$379.1 billion overall.
- It will finish the year with a \$731.5 billion balance.

Near-term, this income surplus continues (revenues and interest), reaching \$2.892 trillion in 2018. However, in 2012 outlays (\$861.4 billion) will exceed tax revenues (\$852.3 billion) — that's just four years beyond CBO's current 10-year projection window. Social Security's total exhaustion is projected for 2029 (Social Security would then be able to pay only 75 percent of the benefits). Saving a dollar now in no way changes that future dynamic.

The Social Security Trust Fund and the Federal Budget

As evident above, according to CBO estimates, the Social Security trust fund now produces a large surplus for the overall federal budget (\$100.6 billion in 1998) and this will continue to grow, reaching \$197.4 billion in 2008. In short, over the entire CBO projection period of FY98-08, the federal budget will never be in balance excluding this surplus. Clinton's Office of Management and Budget does not disagree.

It is important to recall that President Clinton is not talking about saving the surplus the Social Security program is running — a figure far higher than the budget surplus he projects.

- The Clinton budget projects a federal budget surplus of \$220 billion over FY99-03.

- The Clinton budget projects Social Security's revenues will exceed its outlays by \$305.1 billion over FY99-03.

The "Doability" Issue: Where Would the "Saved Surplus" Go?

As explained above, there is no place for Social Security receipts except the Social Security trust fund. The law requires that they be deposited in government securities. And so, where would the "saved surplus" go?

- Would it mean the creation of a second trust fund to back up the current one? Some Democrats in the House have actually proposed this (HR 3207). However, this doesn't change the program's basic dynamic: paying current benefits with current taxes — not pre-funding future benefits. The process of having to redeem securities in the future, when current tax revenues will be insufficient to do so, still holds — no matter how many trust funds are created.
- Would it mean simply stacking currency in a vault? While not a serious proposal, it has the advantage over the backup trust fund approach in that this would at least guarantee that the money actually would be there in the future.
- Would it mean investing in the private sector? Not unless the law is changed.

Both the unrealistic proposals — House Democrats' backup trust fund plan and the idea of squirreling it away in a vault — point at a very serious fact: The system as it is now constructed cannot fund its future liabilities and cannot "save" for the future any of the surplus it is now generating.

The Social Security "Trust Fund" is not a Real Trust Fund

The crucial difference between the Social Security trust fund and a true trust fund is this: In a trust fund held by a private person, current dollars are used to fund future needs *by virtue of investment*. This investment creates more wealth — some of which is returned to the individual as interest, dividends, etc. Thus the privately held trust fund not only returns the money initially deposited but more. In short, it creates additional wealth.

In contrast, the Social Security trust fund cannot even conserve wealth (return the initial deposit of a surplus) much less create more.

Government is Not a Bank

The key is that government does not invest — it simply taxes, spends, and controls the supply of money. Of course, some of this activity has an impact on economic growth. Yet the fact remains: the money it "saves" it merely spends. Money is not there for the future (because it is spent) and is not around in greater quantity (because it is not invested).

The money that is saved — i.e., running a surplus — is merely purchasing debt. Assuming this is Clinton's plan, the federal debt that would be purchased would merely be shifted from private sector holding to public sector holding (the Social Security trust fund). And so, total debt would not fall (it actually increases because Social Security's surplus over and above the federal budget surplus requires the issuance of additional securities to the trust fund).

What Does "Saving the Surplus for Social Security" Do Economically?

Since the Social Security trust fund cannot directly create its own wealth — as can a private trust fund — the question of what effect "saving the surplus" would have on the overall economy is crucial. This is because it is the overall economy that, without reform, inevitably will have to support the coming burden on the Social Security trust fund when its pay-as-you-go system is unable to pay.

If the Social Security trust fund does not either directly conserve or create wealth, would "saving the surplus" do so indirectly? Very little if at all, although it is certainly better than increasing government spending. The greater economic effect of "saving the surplus" is negative and arises from the removal of more money from the private sector (the "surplus") than is needed to run the government. The lesser economic effect of "saving the surplus" is positive and arises from not only eliminating federal borrowing but actually buying back debt from the public — this in turn creates "extra" money available for lending, thus lowering interest rates.

Yet there are reasons why the positive benefits of interest rate reductions will be mitigated: 1) global demand for capital is expected to remain high, thus keeping pressure on domestic interest rates, and 2) interest rates are built on future expectations, and these cannot be sanguine considering the looming fiscal pressure of Social Security and other entitlement spending growth.

And so, while "saving the surplus" will have no impact on the Social Security trust fund being able to meet its future liabilities, it will also have little indirect effect on enabling the economy to help in the situation.

Clinton's Proposal: Dishonestly and Dangerously Meaningless

President Clinton's proposal to *"save Social Security first"* reserving *"100 percent of the surplus"* is substantively meaningless. First, Clinton is not planning to save all of the possible surplus — his new spending takes \$150 billion that could have been so used. Second, the surplus cannot be saved in any case — not literally and certainly not to pay for future Social Security costs. The *only* way the budget surplus could be used the way in which Clinton appears to promise is to truly invest it in the private sector — such as in some type of individually held, government-administered accounts.

However, Clinton's proposal is more than simply meaningless and dishonest. It is also dangerous. It is dangerous because it gives the impression that it does all the things it implicitly claims to do. It thereby undercuts the urgency in attending to both Social Security reform and overall entitlement reform. Once again, the President is promising more than he delivers.

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